Supreme Court, U.S.
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No. 87-846

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

In re KENDAVIS HOLDING COMPANY AND KENDAVIS INDUSTRIES INTERNATIONAL, INC.,

Debtors

K.W. DAVIS, JR., ALANA LAWLER, ALANA LAWLER TRUST "A", A.T. DAVIS, A.T. DAVIS TRUST "A", KAY DAVIS, KAY DAVIS TRUST "A", TRICIA KAE LAWLER, ALANA LAWLER CHILDREN'S TRUST, ALLEN KENNETH DAVIS, JANIECE BREANNE DAVIS, A.T. DAVIS CHILDREN'S TRUST, KAY DAVIS CHILDREN'S TRUST, T.C. DAVIS, II, T.C. DAVIS, II TRUST, T.C. DAVIS, II TRUST "A", T.C. DAVIS, II TRUST "A" DATED JANUARY 15, 1982, BRIAN KEITH DAVIS, BRIAN KEITH DAVIS TRUST, BRIAN KEITH DAVIS TRUST "A", BRIAN KEITH DAVIS TRUST DATED JANUARY 15, 1982, CHESLEY DAVIS, CHESLEY DAVIS TRUST, TREY DAVIS, TREY DAVIS TRUST, KEN W. DAVIS FOUNDATION, AND TWALLA DUPRIEST, TRUSTEE FOR ESTATE OF T.C. DAVIS,

Petitioners

v.

THE OFFICIAL UNSECURED CREDITORS' COMMITTEES FOR KENDAVIS HOLDING COMPANY AND KENDAVIS INDUSTRIES INTERNATIONAL, INC., KENDAVIS HOLDING COMPANY, FEDERAL DEPOSIT INSURANCE CORPORATION, BANK OF NOVA SCOTIA, AND MBANK HOUSTON, N.A.,

Respondents

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF OF RESPONDENT THE BANK OF NOVA SCOTIA IN OPPOSITION

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Rule 28.1 Listing of Parents, Subsidiaries and Affiliates of The Bank of Nova Scotia

The Bank of Nova Scotia Jamaica Limited
The Bank of Nova Scotia Trust Company Jamaica Limited
The Bank of Nova Scotia Trust Company of New York
The Bank of Nova Scotia Trinidad & Tobago Limited
The Bank of Nova Scotia Trust Company of Trinidad and Tobago Limited
Banc-Merc Investment Group Inc.
Brunswick Square Limited
Canborough Limited
The Canborough Corporation
Caribbean Credit Corporation N.V.
Caribbean Credit Corporation (Curacao) N.V.
Caribbean Mercantile Bank N.V.
Chargex Limited
Export Finance Corporation of Canada Limited
Fredericton Developments Limited
Kings Place Parking Limited
ICIC Holdings Limited
Industrial Credit Insurance Company
Maduro & Curiel's Bank N.V.
Maduro & Curiel's Bank (Bonaire) N.V.
Maduro & Curiel's Insurance Services N.V.
N.V. De Curacaosche Hypotheekbank
N.V. De Spaar En Beleenbank Van Curacao
N.V. Trust—En Administratie Maatschappij Van Maduro & Curiel's Bank N.V.
Progress N.V.
Scotia Centre Limited
Scotia Mortgage Corporation
Scotia-Toronto Dominion Leasing Limited
Scotiabank de Puerto Rico
The West India Company of Merchant Bankers Limited
The Windward Islands Bank Limited

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BRIEF OF RESPONDENT THE BANK OF NOVA SCOTIA IN OPPOSITION

STATEMENT OF THE CASE AND SUMMARY OF ARGUMENT

These cases were commenced by the filing of involuntary petitions for reorganization in the United States Bankruptcy Court for the Northern District of Texas on February 21, 1985, and orders for relief were entered by consent on March 11 and 13, 1985. It was not

until November 24, 1986 that the Creditors' Committees' Plan of Reorganization was confirmed by order of Bankruptcy Judge McGuire, affirmed by District Judge Fish on March 26, 1987 and consummated on April 16, 1987.

The Bank of Nova Scotia is the largest creditor of the debtors, being owed $67,235,555.78 in principal amount. One of the major bank creditors and an active participant in the reorganization case was Morgan Guaranty Trust Company of New York ("Morgan Guaranty"). Petitioners are the former stockholders of the admittedly insolvent debtors.

After having shepherded this case through more than a year and a half of intense negotiations and litigation, on March 23, 1987, Bankruptcy Judge McGuire informed counsel that he had the night before learned that Morgan Guaranty was a wholly owned subsidiary of J.P. Morgan & Co. Incorporated ("J.P. Morgan"), in which he held approximately $36,000 of common stock as trustee for himself and his family. He immediately recused himself from further proceedings in the cases, which were assigned to Bankruptcy Judge Harold C. Abramson. Judge McGuire stated on the record, and there is no reason to doubt, that he did not know of the existence of the conflict raised by J.P. Morgan's ownership of Morgan Guaranty until the time that he informed counsel.

Petitioners do not quarrel with any of the above nor with Judge McGuire's immediate recusal; instead they seek to void orders of confirmation of plans of reorganization in these cases. To accomplish what? To vindicate a statute in which "knows" is the operative word? To punish a Bankruptcy Judge who acted immediately upon learning the facts? Or is it just to reargue on remand points that the Court of Appeals for the Fifth Circuit held to be "frivolous"? Indeed, since the debtor corporations are admittedly insolvent, rendering their stock worthless, these Petitioners lack standing on remand and in fact now do not have any financial stake in the outcome of these cases.

As the party with the largest stake in these proceedings, The Bank of Nova Scotia urges this Court to deny certiorari and finally to put an end to this litigation.

ARGUMENT

I

JUDGE McGUIRE FULLY COMPLIED WITH SECTION 455

Immediately upon learning of his financial interest in the parent of Morgan Guaranty, Judge McGuire recused himself. Thus, he fully complied with both Sections 455(a) and 455(b)(4).

Petitioners try two stratagems to get around that fact. The first is to argue that, despite the fact that Judge McGuire did not know of his indirect financial interest in a creditor before March 23, 1987, an objective observer could think that he did creating an appearance of impropriety. That argument is flawed because it would read the knowledge requirement out of Section 455(b)(4). There is nothing in the legislative history to suggest that Congress placed the phrase "he knows" in the statute merely to have it ignored. Section 455 is structured so that (i) a judge must disqualify himself when there is a reasonable question as to his impartiality and (ii) "[h]e shall *also* disqualify himself . . . [when] [h]e *knows* that he . . . has a financial interest." [Emphasis added.] The language of the statute indicates that financial interest is a separate ground for disqualification covered only by subsection (b)(4).

While, as Petitioners claim, "the theme [of the legislative history] is the promotion and protection of public and litigant confidence in the impartiality of judicial decisions," Petitioners' Brief at 9, it does not promote or protect anyone's interest to void decisions rendered by judges who did not even know they had a basis for a bias. No court has done this. There is no need for this Court to take this case and impose such a rule for the first time.

Moreover, even the "constructive knowledge" or "objective observer" standard of the Fifth Circuit, which is already before this Court in *Health Services Acquisition Corp. v. Liljeberg*, 796 F.2d 796 (5th Cir. 1986), *cert. granted*, 107 S. Ct. 1368 (1987), was satisfied in this case. Judge McGuire on taking this case inquired of his stockbroker, who he thought was an authoritative source as to whether there was any connection between Morgan Stanley and J.P. Morgan. After a busy judge received an assurance that there was no such connection, it cannot be said that an objective person would expect him to inquire further. Thus, the District Court specifically found that an objective observer would not quarrel with Judge McGuire's behavior. P. Appendix at 15-16. The Fifth Circuit has correctly emphasized that "[w]here a reasonable person would only speculate that a judge might have actual knowledge of the

facts, constructive knowledge does not exist." *Health Services*, 796 F.2d at 803.

Finally, for Petitioners to claim that Judge McGuire's statements were "unsworn" is ludicrous and offensive. If Judge McGuire would misstate the facts before parties to a case and a court reporter, clearly "swearing" would be pointless.

Petitioners' second stratagem to avoid the fact that Judge McGuire complied with Section 455 is to ask this Court to impose a rule that any mistake or lack of full information, regardless of its impact on a judge's decisions or the litigants before him, should be "remedied" by sending all the litigants back to the inception of the case. No court has done this, and it is unnecessary for this Court to consider doing so now.

Section 455(c) provides in relevant part that "[a] judge should inform himself about his personal and fiduciary financial interests." 28 U.S.C. § 455(c). It does not make him an insurer that the information he receives upon an inquiry is infallible. It does not require that, in the event of an error in the judge's information that does not result in actual bias, an enormous burden should be placed on one litigant to the sole benefit of the other.

II

THERE IS NO JUSTIFICATION FOR THE DRASTIC REMEDY THAT PETITIONERS SEEK TO IMPOSE

Petitioners ask the rhetorical question, "[h]ow can the public and losing litigants be satisfied by being told the judge failed to know what he owned?" Petitioners' Brief at 17. The Bank of Nova Scotia submits that the District Court was correct in concluding that the "public," in the guise of the "reasonable person" or "objective observer," would not be shocked or distressed that Judge McGuire was not aware of all the details of what he owned. In fact, The Bank of Nova Scotia submits that the public would lose faith in a judicial process that forced winning litigants to repeat two years of litigation because of an abstract concern with appearances when there is no actual bias. And losing litigants (and especially those whose substantive claims are "frivolous") do not need protection from a judge who has no bias because he lacks any knowledge of why he could, arguably, be biased.

As for the losing litigants in this case, their claims, which they ask this Court to give them the opportunity to relitigate, were described

by the Fifth Circuit as "frivolous." Thus, reversal and remand can only operate to return these cases for relitigation of frivolous contentions. Petitioners indeed have no cause to complain and no stake in the outcome; they are the former shareholders of admittedly insolvent companies that owed Respondent The Bank of Nova Scotia alone over $67,000,000.

Moreover, under the rule and remedy Petitioners ask this Court to impose, winning litigants would have no way to protect themselves from a reversal of all their efforts after two, five or any number of years had passed. In this case, Petitioners could have checked the public disclosure list of Judge McGuire's stock ownership on file in the Bankruptcy Court and, had they known the connection between J.P. Morgan and Morgan Guaranty, moved for recusal. Petitioners did not do so, and they should not be permitted a "free shot" at relitigating their position. Further, in other circumstances, where a judge honestly but mistakenly believed that he did not own stock in a party and hence the ownership did not appear on court records, there would be no way for a winning litigant to protect itself from a later voiding of the judgment it had obtained. Thus, the winning litigant would be prejudiced and yet have been unable to protect itself, and the losing litigant would have the benefit of another attempt to litigate even when it was not actually prejudiced.

CONCLUSION

This Court should not grant certiorari in this case. There is no outstanding cause to be vindicated and no conflict among Circuits to be resolved. There is only the petition of those whose substantive claims are "frivolous," who lack a financial stake in the outcome, and who would further delay the rightful reorganization of corporations with over $500 million of debt.

Respectfully submitted.

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